

Report of the Auditor-General

Ephraim Mogale Local Municipality

30 June 2014

Report of the auditor-general to the Limpopo Provincial Legislature and the council on the Ephraim Mogale Local Municipality

Report on the financial statements

Introduction

1. I was engaged to audit the financial statements of the Ephraim Mogale Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2014, the statements of financial performance, changes in net assets, and cash flows and the statement of comparison of budget information with actual information for the year then ended, as well as the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2013 (Act No. 2 of 2013) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-general's responsibility

3. My responsibility is to express an opinion on the financial statements based on conducting the audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the general notice issued in terms thereof and International Standards on Auditing. Because of the matters described in the basis for disclaimer of opinion paragraphs, however, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for disclaimer of opinion

Financial statements

4. I was unable to obtain sufficient appropriate audit evidence regarding the financial statements as a whole, as the financial statements were presented for audit purposes without accurate and complete underlying accounting records. I was unable to audit the financial statements by alternative means. Consequently I was unable to determine whether any adjustments relating to the financial statements as a whole were necessary.

Unauthorised expenditure

5. The municipality did not include particulars of unauthorized expenditure in note 40 to the financial statements as required by section 125(2)(d) of the MFMA. The municipality incurred expenditure in excess of the budget resulting in unauthorised expenditure being understated

by R61 061 161 (2013: R35 939 552). The municipality did not have adequate systems in place to identify and report on all unauthorised expenditure incurred. Consequently I was unable to determine the full extent of the understatement in unauthorised expenditure as it was impracticable to do so.

Irregular expenditure

6. The municipality did not include particulars of irregular expenditure in note 40 to the financial statements as required by section 125(2)(d) of the MFMA. The municipality made payments in contravention of the supply chain management requirements which were not included in irregular expenditure, resulting in irregular expenditure being understated by R33 223 505 (2013: R35 097 856). The municipality did not have adequate systems in place to identify and report on all irregular expenditure incurred. Consequently I was unable to determine the full extent of the understatement in irregular expenditure as it was impracticable to do so.

Disclaimer of opinion

7. Because of the significance of the matters described in the basis for disclaimer of opinion paragraphs, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on the financial statements.

Emphasis of matter

8. I draw attention to the matter below. My opinion is not modified in respect of the matter.

Restatement of corresponding figures

9. As disclosed in note 39 to the financial statements, the corresponding figures for 30 June 2013 have been restated as a result of an error discovered during 2014 in the financial statements of the municipality at, and for the year ended, 30 June 2013.

Additional matters

10. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Unaudited supplementary schedules

11. The municipality provided supplementary information in the financial statements on whether resources were obtained and used according to the legally adopted budget, in accordance with SA Standards of GRAP 1, *Presentation of financial statements*. The supplementary budget information set out on pages xx to xx does not form part of the financial statements and is presented as additional information. Accordingly, I do not express an opinion thereon.

Unaudited disclosure notes

12. In terms of section 125(2)(e) of the MFMA the municipality is required to disclose particulars of non-compliance with the MFMA. This disclosure requirement did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon.

Withdrawal from the audit engagement

13. Due to the limitation imposed on the scope of the audit by management, I have disclaimed my opinion on the financial statements. But for the legislated requirement to perform the audit of the municipality, I would have withdrawn from the engagement in terms of the ISAs.

Report on other legal and regulatory requirements

14. In accordance with the PAA and the general notice issued in terms thereof, I report the following findings on the reported performance information against predetermined objectives for selected development priorities presented in the annual performance report, non-compliance with legislation as well as internal control. The objective of my tests was to identify reportable findings as described under each subheading but not to gather evidence to express assurance on these matters. Accordingly, I do not express an opinion or conclusion on these matters.

Predetermined objectives

15. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected development priority presented in the annual performance report of the municipality for the year ended 30 June 2014:
- Basic Service Delivery on pages xx to xx
16. I evaluated the reported performance information against the overall criteria of usefulness and reliability.
17. I evaluated the usefulness of the reported performance information to determine whether it was presented in accordance with the National Treasury's annual reporting principles and whether the reported performance was consistent with the planned development priority. I further performed tests to determine whether indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's *Framework for managing programme performance information* (FMPPI).
18. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
19. The material findings in respect of the selected development priority are as follows:

Basic service delivery

Usefulness of reported performance information

20. Section 41(c) of the Municipal Systems Act, 2000 (Act no. 32 of 2000) (MSA) requires the integrated development plan to form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 100% of the reported objectives, 76% of the reported indicators and a total of 71% of the reported targets were not consistent with those in the approved integrated development plan. This was due to a lack of proper systems and processes for performance management.
21. The FMPPI requires the following:
- The period or deadline for delivery of targets must be specified. No (100%) targets were time bound.

- Performance indicators must be well defined by having clear data definitions so that data can be collected consistently and is easy to understand and use. None (100%) of the indicators were well defined.
 - Performance indicators must be verifiable, meaning that it must be possible to validate the processes and systems that produced the indicator. A total of 22% of the indicators were not verifiable.
22. This was because management did not adhere to the requirements of the FMPPI due to a lack of proper systems and processes and technical indicator descriptions.
23. The FMPPI requires indicators to relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives. All (100%) of the indicators did not relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives as per the integrated development plan. This was because proper performance planning and management practices had not been developed and implemented to provide for the development of performance indicators and targets included in the integrated development plan.

Reliability of reported performance information

24. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. The reported performance information was not valid, accurate and complete when compared to the source information or evidence provided. This was due to a lack of standard operating procedures or documented system descriptions for the accurate recording of actual achievements and technical indicator descriptions for the accurate measurement, recording and monitoring of performance, monitoring of the completeness of source documentation in support of actual achievements and frequent review of the validity of reported achievements against source documentation.

Additional matters

25. I draw attention to the following matters:

Achievement of planned targets

26. Refer to the annual performance report on pages xx to xx for information on the achievement of the planned targets for the year. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information for the selected programmes reported in paragraphs xx to xx of this report.

Unaudited supplementary information

27. The supplementary information set out on pages xx to xx does not form part of the annual performance report and is presented as additional information. I have not audited these schedules and, accordingly, I do not report thereon.

Compliance with laws and regulations

28. I performed procedures to obtain evidence that the municipality had complied with applicable legislation regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA, are as follows:

Strategic planning and performance management

29. The annual performance report for the year under review did not include the performance of the municipality and each external service provider, a comparison of the performance with set targets, a comparison with the previous financial year and measures taken to improve performance as required by section 46(1)(a), (b) and (c) of the MSA.
30. The annual performance agreements for the municipal manager and all senior managers are not linked to the measurable performance objectives approved with the budget and to the service delivery budget implementation plan as required in terms of section 53(1)(c)(iii) of the MFMA and section 57(1)(b) of the MSA.
31. The performance management system and related controls were not in place as it did not describe and represent the processes of performance planning, monitoring, measurement, review, reporting, improvement and how it is conducted, organised and managed, including determining the roles of the different role-players, as required by sections 38 of the MSA and regulation 7 of the *Municipal planning and performance management regulations*.

Budgets

32. Expenditure was incurred in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of section 15 of the MFMA.

Annual reports and financial statements

33. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements identified by the auditors in the submitted financial statements were not adequately corrected and the supporting records could not be provided subsequently, which resulted in the financial statements receiving a disclaimer audit opinion.

Audit committee

34. The audit committee did not review all the quarterly internal audit reports on performance measurement, as required by *Municipal planning and performance management regulation 14(4)(a)(i)*.
35. The audit committee did not submit, at least twice during the financial year, an audit report on the review of the performance management system to the council, as required by *Municipal planning and performance management regulation 14(4)(a)(iii)*.

Expenditure management

36. An effective system of expenditure control, including procedures for the approval, authorisation, withdrawal and payment of funds, was not in place, as required by section 65(2)(a) of the MFMA.
37. An adequate management, accounting and information system was not in place which recognised expenditure when it was incurred, accounted for creditors and accounted for when payments made, as required by section 65(2)(b) of the MFMA.
38. Reasonable steps were not taken to prevent unauthorised expenditure, irregular expenditure and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

Revenue management

39. An adequate management, accounting and information system which accounts for revenue, debtors and receipts of revenue was not in place, as required by section 64(2)(e) of the MFMA.
40. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the MFMA.
41. Revenue due to the municipality was not calculated on a monthly basis, as required by section 64(2)(b) of the MFMA.
42. Accounts for service charges were not prepared on a monthly basis, as required by section 64(2)(c) of the MFMA.
43. Interest was not charged on all accounts in arrears, as required by section 64(2)(g) of the MFMA.

Procurement and contract management

44. Quotations were accepted from prospective providers who are not registered on the list of accredited prospective providers and do not meet the listing requirements prescribed by the Supply Chain Management (SCM) policy in contravention of SCM regulation 16(b) and 17(b).
45. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM regulation 36(1).
46. Invitations for competitive bidding were not always advertised for a required minimum period of days, as required by SCM regulation 22(1) and 22(2).
47. Bid adjudication was not always done by committees which were composed in accordance with SCM regulation 29(2).
48. Contracts and quotations were awarded to bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).
49. Construction contracts were awarded to contractors that were not registered with the Construction Industry Development Board (CIDB), in accordance with section 18(1) of the Construction Industry Development Board Act, 2000 (Act no. 38 of 2000) (CIDB Act) and CIDB regulations 17 and 25(7A).
50. Construction projects were not always registered with the CIDB, as required by section 22 of the CIDB Act and CIDB regulation 18.
51. The performance of contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.
52. The contract performance and monitoring measures and methods were insufficient to ensure effective contract management, as required by section 116(2)(c) of the MFMA.
53. Persons in the service of the municipality who had a private or business interest in contracts awarded by the municipality failed to disclose such interest, as required by SCM regulation 46(2)(e), the code of conduct for councillors issued in terms of the MSA and the code of conduct for staff members issued in terms of the MSA.
54. Bids were not always evaluated by bid evaluation committees which were composed of officials from the departments requiring the goods or services AND/OR at least one SCM practitioner of the municipality as required by SCM regulation 28(2).

Asset management

55. An effective system of internal control for assets (including an asset register) was not in place, as required by section 63(2)(c) of the MFMA.

Human resource management

56. An acting CFO was appointed for a period of more than six months, in contravention of section 54A(2A) and 56(1)(c) of the MSA.
57. The municipality did not develop and adopt appropriate systems, policies and procedures to monitor, measure and evaluate performance of staff in contravention of MSA section 67(d).
58. The municipal manager and senior managers directly accountable to the municipal manager did not sign performance agreements, as required by section 57(2)(a) of the MSA.

Conditional grants management

59. The municipality did not evaluate its performance in respect of programmes or functions funded by the Municipal Infrastructure Grant allocation, as required by section 12(5) of the DoRA.

Consequence management

60. Unauthorised, irregular, fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a)(ii) of the MFMA.

Internal control

61. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with legislation. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for disclaimer of opinion, the findings on the annual performance report and the findings on non-compliance with legislation included in this report.

Leadership

62. The accounting officer does not perform adequate review and monitoring of the financial and performance reporting. This has resulted in the financial statements and the annual performance report containing material misstatements.
63. The action plan developed by the municipality to address internal and external audit findings is not adequate to ensure that root causes that resulted in the findings are resolved.

Financial and performance management

64. The municipality did not have a proper record management system to maintain information that supports the financial statements and reported performance contained in the annual performance report.
65. The accounting officer did not adequately review and monitor compliance with laws and regulations resulting in irregular, fruitless and wasteful and unauthorised expenditure.
66. The significant number of adjustments to the PPE balances and qualification paragraphs

would be attributable to capacity constraints in the Asset management unit.

Governance

67. The audit committee did not ensure that there is an adequately resourced and functioning internal audit unit that identifies internal control deficiencies and recommends corrective action effectively.

Other reports

Investigations

68. An investigation was performed against the former acting chief financial officer that allegedly forged the signature of the former municipal manager on a contract.

Auditor-General

Polokwane

28 November 2014



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence